Supreme Court, U.S.
FILED
MAY 20 1978
MICHAEL RODAK, JR., CLERK

No. 77-1098

In the Supreme Court of the United States

OCTOBER TERM, 1977

HARVEY L. BELL, PETITIONER

v.

INTERNATIONAL TRADING, LTD., ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF ARKANSAS

BRIEF FOR THE COMMODITY FUTURES TRADING COMMISSION AS AMICUS CURIAE

WADE H. MCCREE, JR.,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

JOHN G. GAINE,
General Counsel,

RICHARD E. NATHAN,
Deputy General Counsel,

FREDERIC T. SPINDEL,
Associate General Counsel,
Commodity Futures Trading Commission,
Washington, D.C. 20581.

INDEX

	Page
Question presented	1
Statement	2
Discussion	3
Conclusion	~~15~~ 14

CITATIONS

Cases:

British American Commodity Options Corp. v. *Bagley*, 552 F.2d 482, certiorari denied, No. 77-96, November 7, 1977	2
Burbank v. *Lockheed Air Terminal, Inc.*, 411 U.S. 624	8
Campbell v. *Hussey*, 368 U.S. 297	7
Case & Co. v. *Board of Trade*, 523 F.2d 355	5
Clayton Brokerage Co. v. *Mouer*, 531 S.W.2d 805, dismissing as moot, 520 S.W.2d 802	3
Florida Lime & Avocado Growers, Inc. v. *Paul*, 373 U.S. 132	8
Georgia v. *Pennsylvania R. Co.*, 324 U.S. 439	5
Goodman v. *H. Hentz & Co.*, 265 F. Supp. 440	5
Hawaii v. *Standard Oil Co. of California*, 405 U.S. 251	5
Jones v. *Rath Packing Co.*, 430 U.S. 519	8
Kelley v. *Carr*, CCH Comm. Fut. L. Rep. ¶ 20,517, appeal pending, C.A. 6, Nos. 78-1091 to 78-1093	4-5

Cases—Continued

	Page
Missouri v. *Illinois & Chicago District*, 180 U.S. 208	5
Pennsylvania v. *West Virginia*, 262 U.S. 553	5
Regional Rail Reorganization Act Cases, 419 U.S. 102	13
Rice v. *Santa Fe Elevator Corp.*, 331 U.S. 218	7, 11, 13
State by Spannus v. *Coin Wholesalers, Inc.*, 250 N.W.2d 583	4
Texas v. *Monex International, Limited*, 527 S.W.2d 804, writ refused, No. B-5658	3
United States v. *Philadelphia National Bank*, 374 U.S. 321	13
Waterman Steamship Corp. v. *United States*, 381 U.S. 252	13

Statutes and regulations:

Commodity Exchange Act, 42 Stat. 998, as amended by the Commodity Futures Trading Commission Act, 88 Stat. 1389, 7 U.S.C. 1 *et seq.*	2, 3, 5, 6
Section 2(a)(1), 7 U.S.C. 2	2, 6
Section 4b, 7 U.S.C. 6b	9, 10, 11
Section 4c, 7 U.S.C. (1970 ed.) 6c	8
Section 4c, 7 U.S.C. 6c, as amended by Section 402(d), 88 Stat. 1413	9, 10, 11, 14
Section 4c(b), 7 U.S.C. 6c(b)	6, 7, 9
United States Warehouse Act, 39 Stat. 486, as amended, 7 U.S.C. 241 *et seq.*	11

Statutes and regulations—Continued

	Page
Arkansas Securities Act of 1959:	
Section 1, Ark. Stat. Ann. 1947, § 67-1235 (1966 Repl.)	2
Section 13(*l*), Ark. Stat. Ann. 1947, § 67-1247(*l*) (1966 Repl.)	2
17 C.F.R. 32.9	9
Miscellaneous:	
120 Cong. Rec. 30464 (1974)	11
40 Fed. Reg. 26505	14
43 Fed. Reg. 16153	4
43 Fed. Reg. 16153-16166	4
H.R. 10285, 95th Cong., 2d Sess. (1978)	4
H.R. Rep. No. 93-975, 93d Cong., 2d Sess. (1974)	6, 9
Johnson, *The Commodity Futures Trading Commission Act: Preemption as Public Policy*, 29 Vand. L. Rev. 1 (1976)	9
S. 2391, 95th Cong., 2d Sess. (1978)	4
S. Rep. No. 93-1131, 93d Cong., 2d Sess. (1974)	6, 7, 11
S. Conf. Rep. No. 93-1194, 93d Cong., 2d Sess. (1974)	6, 7, 10, 14
S. Rep. No. 94-73, 94th Cong., 1st Sess. (1975)	12, 13

In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1098

HARVEY L. BELL, PETITIONER

v.

INTERNATIONAL TRADING, LTD., ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF ARKANSAS

BRIEF FOR THE COMMODITY FUTURES TRADING COMMISSION AS AMICUS CURIAE

This brief is filed in response to the Court's invitation of March 27, 1978.

QUESTION PRESENTED

Whether the Commodity Exchange Act, as amended, 7 U.S.C. 1 *et seq.*, precludes the states from applying the antifraud provisions of state securities laws to commodity futures options transactions.

STATEMENT

The case arose when petitioner, the Securities Commissioner for the State of Arkansas, filed suit in Arkansas state court alleging that respondents had violated Section 1 of the Arkansas Securities Act of 1959, Ark. Stat. Ann. 1947, § 67-1235 (1966 Repl.), in connection with the sale in Arkansas of certain commodity future options.[1] Petitioner contended that the commodity futures options were "securities" under Section 13(*l*) of the Arkansas Securities Act, Ark. Stat. Ann. 1947, § 67-1247(*l*) (1966 Repl.), and sought an injunction restraining respondents from making false and deceptive statements and otherwise engaging in acts and practices proscribed by Section 1 in connection with the offer and sale of these "securities" (Pet. App. 19, 20, 22-23).

The trial court entered judgment for petitioner, but the Supreme Court of Arkansas reversed and ordered dismissal of the suit. The State supreme court held (Pet. App. 25-26) that the amendment enacted in 1974 to Section 2(a)(1) of the Commodity Exchange Act, 88 Stat. 1389, 7 U.S.C. 2, and its legislative history, manifested a "clear intention to

[1] A commodity option is a contractual right to buy, or sell, a commodity or commodity future by some specific date at a specified price. So-called "London options," such as those the respondents sold, are options on futures contracts for certain commodities that are traded on exchanges and markets in London, England. *British American Commodity Options Corp.* v. *Bagley*, 552 F.2d 482, 484-485 (C.A. 2), certiorari denied, No. 77-96, November 7, 1977. See also Pet. App. 23-25.

vest exclusive jurisdiction of the regulation of commodity options in the Commodity Futures Trading Commission and to supersede the jurisdiction of all state and federal agencies." The court concluded that the trial court was without jurisdiction to act under the Arkansas Securities Act, and that petitioner had no standing to bring the suit (Pet. App. 30).

DISCUSSION

1. The petition does not present a question warranting review by this Court.

a. The ruling of the Arkansas Supreme Court does not conflict with the decisions of any state or federal court. Indeed, all other courts that have considered whether the states are precluded by the 1974 amendments to the Commodity Exchange Act from regulating commodity futures agreements have reached the same conclusion as the Arkansas court.[2] See *Clayton Brokerage Co.* v. *Mouer*, 531 S.W.2d 805, 806 (Tex.), dismissing as moot, 520 S.W.2d 802 (Tex. Civ. App.); *Texas* v. *Monex International, Limited*, 527 S.W.2d 804, 806-807 (Tex. Civ. App.), writ refused, No. B-5658 (Tex.).[3]

[2] In 1974, Congress enacted the Commodity Futures Trading Commission Act, 88 Stat. 1389, amending the Commodity Exchange Act, 42 Stat. 998, 7 U.S.C. 1 *et seq.* For ease of reference, the Commodity Futures Trading Commission Act is referred to herein as the "1974 amendments" to the Commodity Exchange Act.

[3] It has been held that where retrospective relief, rather than injunctive relief, is requested, the states may apply local

b. The practical significance of the ruling below is insubstantial. The Commodity Futures Trading Commission has suspended all offers and sales of commodity options to the general public effective June 1, 1978. 43 Fed. Reg. 16153-16166.[4] Furthermore, legislation is pending before Congress to provide a statutory ban on transactions in London commodity options, such as are involved in this litigation.[5] In light of the imminent cessation of such commodity option sales to the general public, whether a state possesses authority to enforce an antifraud provision of its securities laws against such sales is not a question of substantial importance.

c. The effect of the decision of the Arkansas court is not, as petitioner asserts (Pet. 14), to make the State powerless to protect its citizens from fraudulent practices in connection with commodity transactions. It has been recognized that a state has standing to sue as *parens patriae* to enjoin violations of the antifraud provisions of the Act. *Kelley* v. *Carr*, CCH Comm. Fut. L. Rep. ¶ 20,517, p. 22,134 decided

---

regulatory prohibitions to commodity transactions completed prior to April 21, 1975, the effective date of the 1974 amendments to the Commodity Exchange Act. *State by Spannus* v. *Coin Wholesalers, Inc.*, 250 N.W.2d 583, 586-587 (Minn.). That court recognized, however, that exclusive Federal jurisdiction exists over commodity transactions completed after that date. *Id.* at 587.

[4] The regulation does not restrict the offer and sale of commodity options to commercial buyers for use in connection with their businesses. See 43 Fed. Reg. 16153.

[5] See S. 2391, 95th Cong., 2d Sess. (1978); H.R. 10285, 95th Cong., 2d Sess. (1978).

December 5, 1977, (W.D. Mich.), appeal pending, Nos. 78-1091 to 78-1093 (C.A. 6).[6] Moreover, the need for such protection is dubious since the citizens of each state are directly protected by the Commodity Exchange Act, which creates a private right of action for its enforcement. See *Case & Co.* v. *Board of Trade*, 523 F.2d 355, 360 (C.A. 7); *Goodman* v. *H. Hentz & Co.*, 265 F. Supp. 440, 446-447 (N.D. Ill.). See also pp. 12-14, *infra*.

2. On the merits, it is the position of the Commodity Futures Trading Commission that the court below correctly held that the 1974 amendments to the Commodity Exchange Act preclude the states from enforcing state laws regulating commodity option transactions.[7]

---

[6] This Court has recognized the standing of a State to sue as *parens patriae* to seek equitable relief for the benefit of its citizens to enjoin violations of federal antitrust law and nuisance activities. See *Hawaii* v. *Standard Oil Co. of California*, 405 U.S. 251; *Georgia* v. *Pennsylvania R. Co.*, 324 U.S. 439; *Pennsylvania* v. *West Virginia*, 262 U.S. 553; *Missouri* v. *Illinois & Chicago District*, 180 U.S. 208.

[7] The action arises in the context of an attempt by the Arkansas Securities Administrator to enforce the antifraud provision of the Arkansas Securities Act with respect to allegedly fraudulent commodity options sales by the respondents, and the assertion by the respondents that the "exclusive jurisdiction" granted to the CFTC in the Commodity Futures Trading Commission Act of 1974 precludes application of the antifraud provision of the Arkansas Securities Act to their activities. Accordingly, the decision of the Arkansas Supreme Court should be construed in light of the factual context in which the case arose, and should not be understood as bearing upon any issue concerning the jurisdiction of the federal Securities and Exchange Commission (SEC).

The Commodity Exchange Act, which establishes a scheme of federal regulation of commodity transactions, was amended in 1974 to extend its coverage and to create the Commodity Futures Trading Commission (CFTC). As part of this legislation, Section 2(a)(1) of the Act was amended to provide:

> [T]hat the [Commodity Futures Trading] Commission shall have exclusive jurisdiction with respect to accounts, agreements (including any transaction which is of the character of, or is commonly known to the trade as, an "option" * * *), and transactions involving contracts of sale of a commodity for future delivery * * *. [7 U.S.C. 2.][8]

At the same time, Congress enacted a new provision, Section 4c(b) of the Act, which broadly prohibits the offer or sale of commodity options

> * * * contrary to any rule, regulation, or order of the [Commodity Futures Trading] Commission prohibiting any such transaction or allowing any such transaction under such terms and

[8] The original House bill had limited the CFTC's exclusive jurisdiction to futures contracts, and retained for the SEC a concurrent jurisdiction over other types of futures agreements. See H.R. Rep. No. 93-975, 93d Cong., 2d Sess. 28-29, 87 (1974). The Senate bill, which Congress adopted, made the CFTC's jurisdiction exclusive over all types of commodity future transactions, including commodity options such as are involved in this case. S.Conf. Rep. No. 93-1194, 93d Cong., 2d Sess. 35 (1974). See S. Rep. No. 93-1131, 93d Cong., 2d Sess. 26 (1974); *id.* at 31 ("The [CFTC] will have exclusive jurisdiction over options trading in commodities (but not in securities)").

> conditions as the Commission shall prescribe * * *. [7 U.S.C. 6c(b).]

The court below correctly concluded (Pet. App. 26) that the plain intention of these provisions of the amended Act is to provide the CFTC with comprehensive authority and exclusive jurisdiction, as regards the states, over the regulation of options and other commodity futures transactions. This intention is confirmed in the reports of the Senate Committee on Agriculture and Forestry and the Conference Committee. These reports observed that the exclusive jurisdiction granted the Commission over all futures transactions supersedes the jurisdiction of all state agencies. S. Rep. No. 93-1131, 93d Cong., 2d Sess. 23 (1974); S. Conf. Rep. No. 93-1194, 93d Cong., 2d Sess. 35 (1974). The Conference Committee emphasized further that the authority granted to CFTC would "preempt the field * * *." *Ibid.* Where the controlling statute so unambiguously confers exclusive regulatory authority upon a federal agency, this Court has repeatedly held that state activity in the field is preempted. See, *e.g.*, *Campbell* v. *Hussey*, 368 U.S. 297, 300-302; *Rice* v. *Sante Fe Elevator Corp.*, 331 U.S. 218, 230, 232-236.[9]

[9] In these circumstances, petitioner's contention (Pet. 14-15) that the antifraud provision of Arkansas' securities law is not inconsistent with the federal scheme, even if true, would be of no moment. As this Court recently reaffirmed in *Jones* v. *Rath Packing Co.*, 430 U.S. 519, 525:

> [W]hen Congress has "unmistakably . . . ordained," * * * that its enactments alone are to regulate a part of

Petitioner claims, however, that, even if the CFTC has exclusive jurisdiction to "regulate" commodity futures transactions, a state may continue to enforce its securities antifraud provisions on the theory that such laws do not involve licensing or otherwise "regulate" commodity transactions (Pet. 14). The 1974 amendments to the Act, and their legislative history, however, demonstrate that the exclusive jurisdiction given the CFTC preempts application of all state securities laws, including state securities anti-fraud laws, to commodity futures transactions.

There is no indication in the legislative history that Congress intended to draw any distinction between a state's authority to "regulate" and its authority to prohibit fraud. Indeed, there is evidence that Congress affirmatively considered and determined that CFTC jurisdiction over commodity transactions would be exclusive with regard to fraud prohibition as well as other types of regulation. Prior to the 1974 amendments, the last sentence of Section 4c of the Act had provided that

> [n]othing in this section or section 4b [of this Act] shall be construed to impair any state law applicable to any transaction enumerated or described in such sections. [49 Stat. 1494, 7 U.S.C. (1970 ed.) 6c].

---

commerce, state laws regulating that aspect of commerce must fall.

Accord, Burbank v. *Lockheed Air Terminal, Inc.*, 411 U.S. 624, 633; *Florida Lime & Avocado Growers, Inc.* v. *Paul*, 373 U.S. 132, 141, 142.

This portion of Section 4c had preserved to the states a parallel authority to prohibit transactions also prohibited under Sections 4b and 4c of the Act. Among the transactions prohibited in Section 4b are the sales of commodity futures contracts wherein any person seeks "to cheat or attempt to cheat or defraud [any other person] * * *." 7 U.S.C. 6b. Similarly, Section 4c prohibits the offer or sale of options on commodity futures "contrary to any rule, regulation or order of the [CFTC] * * *." 7 U.S.C. 6c(b). Congress intended that the CFTC would prohibit fraud in connection with commodity option transactions under the broad authority granted by Section 4c, see H.R. Rep. No. 93-975, 93d Cong., 2d Sess. 31, 36-37 (1974) (setting forth CFTC's broad authority and the history of fraud abuse in commodity options trading),[10] and the CFTC has done so in its regulations, 17 C.F.R. 32.9.[11]

---

[10] Indeed, as respondents have noted (Brief of Respondents in Opposition 3-5), it was the presence of severe fraudulent practices in the offer and sale of commodity options that led to the 1974 amendments and the decision to expand the CFTC's jurisdiction. See also Johnson, *The Commodity Futures Trading Commission Act: Preemption as Public Policy*, 29 Vand. L. Rev. 1, 4 (1976).

[11] 17 C.F.R. 32.9 provides:

> It shall be unlawful for any person directly or indirectly—
>
> (a) To cheat or defraud or attempt to cheat or defraud any other person;
>
> (b) To make or cause to be made to any other person any false report or statement thereof or cause to be entered for any person any false record thereof;

The sentence in Section 4c which had allowed the states a parallel authority to prohibit fraud in commodity transactions was removed by the 1974 amendments to the Act. Section 402(d), 88 Stat. 1413. In removing this savings provision, the Conference Report expressly stated that the states are now barred from applying parallel or supplementary laws with respect to the transactions governed by the CFTC under Sections 4b and 4c of the Act:

> The *Conference* substitute adopts the Senate amendment, including the provision in Section 402(d) of the bill which strikes the last sentence of section 4c of the Commodity Exchange Act. The language being struck provides that "Nothing in this section [section 4c] or section 4b shall be construed to impair any State law applicable to any transaction enumerated or described in such sections."
>
> Under the exclusive grant of jurisdiction to the Commission, the authority in the Commodity Exchange Act (and the regulations issued by the Commission) would preempt the field insofar as futures regulation is concerned. Therefore, if any substantive State law regulating futures trading was contrary to or inconsistent with Federal law, the Federal law would govern. In view of the broad grant of authority to the Commission to regulate the futures trading industry, the Conferees do not contemplate that there will be a need for any supplementary regulation by the States. [S. Conf. Rep. No. 93-1194, *supra*, at 35-36.]

(c) To deceive or attempt to deceive any other person by any means whatsoever; in or in connection with an offer to enter into, the entry into, or the confirmation of the execution of, any commodity option transaction.

Senator Curtis, who sponsored the amendment removing the last sentence of Section 4c, stated that "[a]ll of the transactions referred to in that sentence are covered by the existing act as amended by the [1974] bill," and concluded that it was necessary to remove the sentence "to assure that Federal preemption is complete." 120 Cong. Rec. 30464 (1974).

The CFTC believes that this express legislative history demonstrates that its authority under Sections 4b and 4c of the Act is exclusive,[12] and that the 1974 amendments preclude the States from exercising parallel regulatory authority over fraud in connection with commodity futures transactions. See *Rice* v. *Santa Fe Elevator Corp.*, *supra*, 331 U.S. at 232-234.[13]

[12] See note 8, *supra*.

[13] The facts in *Rice* parallel the instant case. In Rice, this Court held that the United States Warehouse Act, 39 Stat. 486, as amended, 7 U.S.C. 241 *et seq.*, precludes the States from the regulation of grain warehouses. In reaching this conclusion, the Court relied strongly on the fact that the federal Act originally had allowed supplementary state regulation, but had been amended to remove a provision protecting state authority and to provide exclusive jurisdiction to the Secretary of Agriculture. The Court held that the Act "terminat[ed] the dual system of regulation" and concluded that "the matters regulated by the Federal Act cannot be regulated by the States * * *." 331 U.S. at 234. Accordingly, where, as in this case, the subject of the state regulation "is in any way regulated by the Federal Act," the federal authority is preclusive. *Id.* at 236.

Petitioner argues (Pet. 12-13), that it is anomalous to conclude that the 1974 amendments preclude the states from exercising regulatory jurisdiction over fraud in connection with commodity futures transactions because a 1975 Senate report on subsequent legislation states that the exclusive jurisdiction of the CFTC over those transactions

> does not prevent the States from enforcing their criminal antifraud statutes. [S. Rep. No. 94-73, 94th Cong., 1st Sess. 5 (1975).]

There is no anomaly between the congressional intent in 1974 to preclude state jurisdiction over commodity futures transactions and the statement in the 1975 Senate report that enforcement of state "criminal antifraud statutes" is not precluded.

The statement in the 1975 Senate report says only that the states may continue to apply their criminal antifraud statutes to commodity futures transactions. Viewed against the 1974 legislative history that Congress intended the CFTC to have exclusive authority over such transactions, the 1975 statement reflected simply the normal principle that the CFTC's exclusive jurisdiction does not necessarily preempt the entire body of general state legislation that only tangentially affects commodity transactions.[14] See *Rice*

[14] We note also that the 1975 legislation did not concern the substantive provisions of the Act that set forth the exclusive jurisdiction of the CFTC, but was enacted to extend the dates by which the CFTC was to adopt regulations under the Act. See S. Rep. No. 94-73, *supra*, at 3. In this situation, the subsequent legislative history may not be entitled to great weight. See *e.g.*, *Regional Rail Reorganization*

v. *Santa Fe Elevator Corp.*, *supra*, 331 U.S. at 236-238. Exclusive federal authority is not necessarily inconsistent with the states' enforcement of their general criminal fraud statutes or the states' enforcement of federal prohibitions by incorporating those prohibitions, where appropriate, into the states' criminal fraud law.[15] Parallel enforcement efforts of this nature were not clearly precluded by the exclusive jurisdiction provisions of the 1974 amendments. The relevant legislative history prohibits "supplementary regulation" by the states: it does not by its terms also prohibit supplementary enforcement of federal regulations by the states. See S. Rep. No. 93-1194, *supra*, at 36.

But the possible application of general criminal antifraud laws is not presented in this case. Petitioner filed this action seeking civil injunctive relief under the authority of the State's specific securities regulation law (Pet. 5).[16] Any possible inconsistency

Act Cases, 419 U.S. 102, 132; *Waterman Steamship Corp.* v. *United States*, 381 U.S. 252, 269; *United States* v. *Philadelphia National Bank*, 374 U.S. 321, 348-349.

[15] Similarly, there is no necessary inconsistency with exclusive federal authority when the State sues as *parens patriae* to enjoin conduct that violates commodity trading regulations established by the CFTC. See p. 4, *supra*.

[16] Arkansas seeks enforcement of a state regulation based on Section 10b-5 of the SEC regulations, 17 C.F.R. 240.10b-5. The antitfraud regulation adopted by CFTC, note 10 *supra*, contains different language, expressly to avoid "uncritical application of securities laws, principles and practices." 40 Fed. Reg. 26505.

between the 1974 legislative history and the 1975 Senate report does not indicate that Congress has repealed or modified Section 402(d) of the 1974 amendments by reinstating authority in the states to engage in supplementary regulation of commodity futures transactions.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

WADE H. MCCREE, JR.,
Solicitor General.

JOHN G. GAINE,
General Counsel,

RICHARD E. NATHAN,
Deputy General Counsel,

FREDERIC T. SPINDEL,
Associate General Counsel,
Commodity Futures Trading Commission.

MAY 1978.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1978 265216 14